



Testimony

Before the Subcommittee on Military Readiness,
Committee on Armed Services,
House of Representatives

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COMMERCIAL ACTIVITIES PANEL

Improving the Sourcing Decisions of the Federal Government

Statement of David M. Walker
Comptroller General of the United States and
Chair of the Commercial Activities Panel



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Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to participate in the subcommittee's hearing on the report of the congressionally mandated Commercial Activities Panel (the Panel). The Panel's work was the result of a provision contained in the Fiscal Year 2001 Defense Authorization Act, which called for me, in my capacity as the Comptroller General, to convene a panel of experts to study, and make recommendations for improving, the policies and procedures governing the transfer of commercial activities for the federal government from government to contractor personnel. The impetus for this legislation was the growing controversy surrounding competitions conducted under Office of Management and Budget (OMB) Circular A-76 to determine whether the government should obtain commercially available goods and services from the public or private sectors.¹ As noted in the introduction to the Panel's report, the use of cost comparison studies under A-76 was under fire from all sides. All parties concerned—federal managers, employees, and industry representatives—were expressing growing frustration with the process, and many believed the process needed significant reform. The Panel's report was published on April 30, 2002, and is available on GAO's Web page at: www.gao.gov under the "Commercial Activities Panel" link.

Controversy surrounding the use of A-76 also occurred at a time of increasing questions over the role of government and who is in the best position to provide needed services. Specifically, should the work of government be performed by government employees, contractors, or a combination of both, possibly through a partnership agreement.

As I have testified on a number of occasions, given recent trends and our long-range fiscal challenges, the federal government needs to engage in a fundamental review, reassessment, and reprioritization of what the government does, how the government does business, and who does the government's business. This is essential in order to increase fiscal flexibility and improve how the government works in the modern world. This drives the need to evaluate and revise the current approach to acquiring commercial services to ensure that it achieves the maximum

¹ Examples of commercial functions typically subject to the competitive sourcing process at the Department of Defense include transportation services, computer services, education and training, and food services.

benefit for the taxpayers and a reasonable balance between a variety of competing interests.

Because of the importance of the issues to be addressed, I chose to chair the Panel rather than to designate someone else, as permitted in the legislation. In my opinion, the Panel's report presents a reasoned, reasonable, and balanced set of recommendations, which, if implemented, would significantly improve the government's sourcing processes and practices. My testimony today provides some context to the Panel's work and then focuses on (1) the processes used to select panel members and other actions taken to ensure a fair and balanced process; (2) the guiding principles, findings, and recommendations of the Panel; and (3) the next steps needed to implement the Panel's recommendations.

Background

Since 1955, the executive branch has encouraged federal agencies to obtain commercially available goods and services from the private sector when the agencies determine that such action is cost-effective. OMB formalized the policy in its Circular A-76, issued in 1966. In 1979, OMB supplemented the circular with a handbook that included procedures for competitively determining whether commercial activities should be performed in-house, by another federal agency through an interservice support agreement, or by the private sector. OMB has updated this handbook several times.

Under A-76, commercial activities may be converted to or from contractor performance either by direct conversion or by cost comparison. Under direct conversion, specific conditions allow commercial activities to be moved from government or contract performance without a cost comparison study (e.g., for activities involving 10 or fewer civilians.)² Generally, however, commercial functions are to be converted to or from contract performance by cost comparison, whereby the estimated cost of government performance of a commercial activity is compared with the cost of contractor performance in accordance with the principles and procedures set forth in Circular A-76 and the revised supplemental handbook. As part of this process, the government identifies the work to be performed (described in the performance work statement), prepares an

² For functions performed by Defense Department employees, a number of additional requirements, reports, and certifications are addressed in chapter 146 of title 10 United States Code and in recurring provisions in the department's annual appropriations acts.

in-house cost estimate on the basis of its most efficient organization,³ and compares it with the winning offer from the private sector.

According to A-76 guidance, an activity should not be moved from one sector to the other (whether public to private or vice versa) unless doing so would save at least \$10 million or 10 percent of the personnel costs of the in-house performance (whichever is less). OMB established this minimum cost differential to ensure that the government would not convert performance for marginal savings.

The handbook also provides an administrative appeals process. An eligible appellant⁴ must submit an appeal to the agency in writing within 20 days of the date that all supporting documentation is made publicly available. Appeals are supposed to be adjudicated within 30 days after they are received. Private-sector offerors who believe that the agency has not complied with applicable procedures have additional avenues of appeal. They may file a bid protest with GAO or file an action in a court of competent jurisdiction.⁵

Circular A-76 requires agencies to maintain annual inventories of commercial activities performed in-house. A similar requirement was included in the 1998 Federal Activities Inventory Reform (FAIR) Act, which directs agencies to develop annual inventories of their positions that are not inherently governmental.⁶ The fiscal year 2001 inventory identified approximately 841,000 full-time equivalent commercial-type

³ The most efficient organization is the government's in-house organization to perform a commercial activity. It may include a mix of federal employees and contract support. It is the basis for all government costs entered on the cost comparison form. It is the product of the management plan and is based upon the performance work statement.

⁴ An eligible appellant is defined as (1) federal employees (or their representatives) and existing federal contractors affected by a tentative decision to waive a cost comparison; (2) federal employees (or their representatives) and contractors who have submitted formal bids or offers and who would be affected by a tentative decision; or (3) agencies that have submitted formal offers to compete for the right to provide services through an interservice support agreement.

⁵ Federal employees do not have standing to file a protest with GAO and have generally been denied standing to sue in court.

⁶ Section 5 of P.L. 105-270, codified at 31 U.S.C. 501 note (1998), defines an inherently governmental function as a "function that is so intimately related to the public interest as to require performance by Federal Government employees."

positions, of which approximately 413,000 were in the Department of Defense (DOD).⁷

DOD has been the leader among federal agencies in recent years in its use of OMB Circular A-76; the Circular's use by other agencies has been very limited. However, in 2001, OMB signaled its intention to direct greater use of the circular on a government-wide basis. In a March 9, 2001, memorandum, OMB directed agencies to take action in fiscal year 2002 to directly convert or complete public-private competitions of not less than 5 percent of the full-time equivalent positions listed in their FAIR Act inventories. Subsequent guidance expanded the requirement to 15 percent in fiscal year 2003, with the ultimate goal of competing at least 50 percent.

Although comprising a relatively small portion of the government's overall service contracting activity, competitive sourcing under Circular A-76 has been the subject of much controversy because of concerns about the process raised both by the public and private sectors. Federal managers and others have been concerned about the organizational turbulence that typically follows the announcement of A-76 studies. Government workers have been concerned about the impact of competition on their jobs, the opportunity for input into the process, and the lack of parity with industry offerors to protest A-76 decisions. Industry representatives have complained about unfairness in the process and the lack of a level playing field between the government and the private sector in accounting for costs. Concerns have also been raised about the adequacy of the oversight of subsequent performance, whether the work is being performed by the public or private sector.

Amid these concerns over the A-76 process, the Congress enacted section 832 of the National Defense Authorization Act for Fiscal Year 2001. The act required the Comptroller General to convene a panel of experts to study the policies and procedures governing the transfer of commercial activities for the federal government from government to contractor personnel. The act also required the Comptroller General to appoint highly qualified and knowledgeable persons to serve on the panel and ensure that the following entities received fair representation on the panel:

⁷ Guidance implementing the FAIR Act permitted agencies to exempt many commercial activities from competitive sourcing consideration on the basis of legislative restrictions, national security considerations, and other factors. Accordingly, DOD's fiscal year 2001 inventory of positions it considered to be potentially subject to competition was reduced to approximately 241,000.

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- DOD.
 - Persons in private industry.
 - Federal labor organizations.
 - OMB.

Appendix I lists the names of the Panel members. The legislation mandating the Panel's creation required that the Panel complete its work and report the results of its study to the Congress no later than May 1, 2002. The Panel's report was published on April 30, 2002.

Steps Taken to Ensure a Representative Panel and a Fair and Balanced Process

In establishing the Panel, a number of steps were taken to ensure representation from all major stakeholders as well as to ensure a fair and balanced process. This began with my selection of Panel members, which was then followed by the Panel's establishment of a process to guide its work.

To ensure a broad array of views on the panel, we used a *Federal Register* notice to seek suggestions on the Panel's composition.⁸ On the basis of the nominations received in response to that notice, as well as the need to include the broad representation outlined in legislation, I personally interviewed a number of potential panel members before selecting other members to serve on the panel. I believe that we selected a group of outstanding individuals representative of diverse interest groups from the public and private sectors, labor unions, academia, and members with experience in dealing with sourcing decisions at the local government level.

⁸ A *Federal Register* notice was also used to solicit public input on issues the panel should address.

Once convened, the Panel, as a group, took a number of steps at the outset to guide its deliberations and ensure a full and balanced consideration of issues. The first step was the adoption of the following mission statement:

Mission of the Commercial Activities Panel

The mission of the Commercial Activities Panel is to improve the current sourcing framework and processes so that they reflect a balance among taxpayer interests, government needs, employee rights, and contractor concerns.

The Panel also agreed that all of its findings and recommendations would require the agreement of at least a two-thirds supermajority of the Panel in order to be adopted. The Panel further decided that each Panel member would have the option of having a brief statement included in the report explaining the member's position on the matters considered by the Panel. In addition to the *Federal Register* notice soliciting input on issues to be considered by the Panel, the Panel held 11 meetings over the period of May 2001 to March 2002, 3 of which were public hearings in Washington, D.C.; Indianapolis, Indiana; and San Antonio, Texas. In the public hearings, Panel members heard testimony from scores of representatives of the public and private sectors, state and local governments, unions, contractors, academia, and others. Panelists heard first-hand about the current process, primarily the cost comparison process conducted under OMB Circular A-76, as well as alternatives to that process. Appendix II provides more detail on the topics and concerns raised at the public hearings. The Panel also maintained an E-mail account to receive written comments from any source.

After the completion of the field hearings, the Panel members met in executive session several times, augmented between meetings by the work of staff to help them (1) gather background information on sourcing trends and challenges, (2) identify sourcing principles and criteria, (3) consider A-76 and other sourcing processes to assess what's working and what's not, and (4) assess alternatives to the current sourcing processes.

Principles, Findings, and Recommendations

As the Panel began its work, it recognized early on the need for a set of principles that would provide a framework for sourcing decisions. Those principles, as they were debated and fleshed out, provided an important vehicle for assessing what does or does not work in the current A-76

process, and provided a framework for identifying needed changes in the process.

Guiding Principles

During its meetings, the Panel coalesced around a set of principles to guide sourcing decisions. The principles helped frame many of the Panel's deliberations and became a reference point for the Panel's work. Moreover, the principles were unanimously adopted by the Panel and included as part of the Panel's recommendations. While each principle is important, no single principle stands alone, and several are interrelated. Therefore, the Panel adopted the principles and their accompanying narrative comments as a package and then used these principles to assess the government's existing sourcing system and to develop additional Panel recommendations.

Guiding Principles for Sourcing Policy

The Panel believes that federal sourcing policy should:

1. Support agency missions, goals, and objectives.
2. Be consistent with human capital practices designed to attract, motivate, retain, and reward a high-performing federal workforce.
3. Recognize that inherently governmental and certain other functions should be performed by federal workers.
4. Create incentives and processes to foster high-performing, efficient, and effective organizations throughout the federal government.
5. Be based on a clear, transparent, and consistently applied process.
6. Avoid arbitrary full-time equivalent or other arbitrary numerical goals.
7. Establish a process that, for activities that may be performed by either the public or the private sector, would permit public and private sources to participate in competitions for work currently performed in-house, work currently contracted to the private sector, and new work, consistent with these guiding principles.
8. Ensure that, when competitions are held, they are conducted as fairly, effectively, and efficiently as possible.
9. Ensure that competitions involve a process that considers both quality and cost factors.
10. Provide for accountability in connection with all sourcing decisions.

The principles and their accompanying commentary are included in their entirety in appendix III.

Findings

The Panel's principles supplied a strong conceptual framework and specific criteria against which to measure any proposals for change in the government's competitive-sourcing policies. The Panel concluded that there are some advantages to the current system. First, A-76 cost comparisons are conducted under an established set of rules, the purpose of which is to ensure that sourcing decisions are based on uniform, transparent, and consistently applied criteria. Second, the A-76 process has enabled federal managers to make cost comparisons between sectors that have vastly different approaches to cost accounting. Third, the current A-76 process has been used to achieve significant savings and efficiencies for the government. Savings result regardless of whether the public or the private sector wins the cost comparison. This is because competitive pressures have served to promote efficiency and improve the performance of the activity studied.

Despite these advantages, the Panel heard frequent criticisms of the A-76 process. The Panel's report noted that both federal employees and private firms complain that the A-76 competition process does not meet the principles' standard of a clear, transparent, and consistently applied process. Since January 1999, GAO has issued 22 decisions on protests involving A-76 cost comparisons. Of these decisions, GAO sustained 11 and denied 11. "Sustaining" a protest means that GAO found that the agency had violated procurement statutes or regulations in a way that prejudiced the protester. Protests involving A-76 represent a very small percentage of the many hundreds of bid protest decisions that GAO issued in the past 3 years. They do, however, indicate an unusually high percentage of sustained protests. In protests decisions covering all procurements, GAO has sustained about one-fifth of the protests, while in A-76 protests, GAO has sustained half. (It should be kept in mind, though, that most A-76 decisions are not protested, just as most contract award decisions are not protested.) These sustained protests generally reflect only the errors made in favor of the government's most efficient organization since only the private-sector offeror has the right to protest to GAO.

While any public-private competition is, by nature, challenging and open to some of the concerns that have been raised regarding the A-76 process, the high rate of successful A-76 protests suggests that agencies have a more difficult time applying the A-76 rules than they do applying the normal (i.e., Federal Acquisition Regulation) acquisition rules. At least in part, this may

be because the Federal Acquisition Regulation (FAR) rules are so much better known. While training could help overcome this lack of familiarity (and many agencies, particularly those in DOD, have been working on A-76 training), the Panel noted that the FAR acquisition and source selection processes are already better known and better understood; they, in a sense, serve as a “common language” for procurements and source selections.

In the Panel’s view, the most serious shortcoming of the A-76 process is that it has been stretched beyond its original purpose, which was to determine the low-cost provider of a defined set of services. Circular A-76 has not worked well as the basis for competitions that seek to identify the best provider in terms of quality, innovation, flexibility, and reliability. This is particularly true in today’s environment, where solutions are increasingly driven by technology and may focus on more critical, complex, and interrelated services than previously studied under A-76. In the federal procurement system today, there is common recognition that a cost-only focus does not necessarily deliver the best quality or performance for the government or the taxpayers. Thus, while cost is always a factor, and often the most important factor, it is not the only factor that may need to be considered. In this sense, the A-76 process may no longer be as effective a tool, since its principal focus is on cost comparisons.

During its year-long study, the Panel identified several key characteristics of a successful sourcing policy. First, the Panel heard repeatedly about the importance of competition and its central role in fostering economy, efficiency, high performance, and continuous performance improvement. The means by which the government utilizes competition for sourcing its commercial functions was at the center of the Panel’s discussions and work. The Panel strongly supported a continued emphasis on competition as a means to improve economy, efficiency, and effectiveness of the government. The Panel also believed that whenever the government is considering converting work from one sector to another, public-private competitions should be the norm. Direct conversions generally should occur only where the number of affected positions is so small that the costs of conducting a public-private competition clearly would outweigh any expected savings. Moreover, there should be adequate safeguards to ensure that activities, entities, or functions are not improperly separated to reduce the number of affected positions and avoid competition.

A second theme consistently cited at the public hearings was the need for a broader approach to sourcing decisions, rather than an approach that

relies on the use of arbitrary quotas or that is unduly constrained by personnel ceilings. Critical to adopting a broader perspective is having an enterprise-wide perspective on service contract expenditures, yet the federal government lacks timely and reliable information about exactly how, where, and for what purposes, in the aggregate, taxpayer dollars are spent for both in-house and contracted services. The Panel was consistently reminded about, and fully agrees with, the importance of ensuring accountability throughout the sourcing process, providing the workforce with adequate training and technical support in developing proposals for improving performance, and assisting those workers who may be adversely affected by sourcing decisions. Improved accountability extends to better monitoring of performance and results after competitions are completed—regardless of the winner.

The Panel heard about several successful undertakings involving other approaches to sourcing decisions. Some involved business process reengineering and public-private partnerships, and emphasized labor-management cooperation in accomplishing agency missions. For example, in Indianapolis, Indiana, on August 8, 2001, the Panel heard from representatives from several organizations that had taken different approaches to the sourcing issue. Among them were the Naval Surface Warfare Center in Crane, Indiana, which reengineered its business processes to reduce costs and gain workshare, and the city of Indianapolis, which effectively used competition to greatly improve the delivery of essential services. In doing so, the city also provided certain technical and financial assistance to help city workers successfully compete for work. These entities endeavored to become “most efficient organizations.” It was from these examples and others that the Panel decided that all federal agencies should strive to become “high performing organizations.”

Third, sourcing policy is inextricably linked to the government’s human capital policies. This linkage has many levels, each of which is important. It is particularly important that sourcing strategies support, not inhibit, the government’s efforts to attract, motivate, and retain a high-performing in-house workforce, as well as support its efforts to access and collaborate with high-performance, private-sector providers. Properly addressed, these policies should be complementary, not conflicting.

Panel Recommendations

In addition to the principles discussed earlier, the Panel adopted a package of additional recommendations it believed would improve significantly the government’s policies and procedures for making sourcing decisions. It is important to emphasize that the Panel decided to

consider and adopt these latter recommendations as a package, recognizing the diverse interests represented on the Panel and the give and take required to reach agreement among a supermajority of the Panelists. As a result, a supermajority of the Panel members recommended the adoption of the following actions:

- *Conduct public-private competitions under the framework of an integrated FAR-based process.* The government already has an established mechanism that has been shown to work as a means to identify high-value service providers: the negotiated procurement process of the Federal Acquisition Regulation. The Panel believes that in order to promote a more level playing field on which to conduct public-private competitions, the government needs to shift, as rapidly as possible, to a FAR-type process under which all parties compete under the same set of rules. Although some changes in the process will be necessary to accommodate the public-sector proposal, the same basic rights and responsibilities would apply to both the private and the public sectors, including accountability for performance and the right to protest. This and perhaps other aspects of the integrated competition process would require changes to current law or regulation (e.g., requirements in title 10 of the U.S. Code that DOD competitive sourcing decisions be based on low cost).
- *Make limited changes to the existing A-76 process.* The development of an integrated FAR-type process will require some time to be implemented. In the meantime, the Panel expects current A-76 activities to continue, and therefore believes some modifications to the existing process can and should be made. Accordingly, the Panel recommended a number of limited changes to OMB Circular A-76. These changes would, among other things, strengthen conflict-of-interest rules, improve auditing and cost accounting, and provide for binding performance agreements.
- *Encourage the development of high-performing organizations (HPOs).* The Panel recommended that the government take steps to encourage HPOs and continuous improvement throughout the federal government, independent of the use of public-private competitions. In particular, the Panel recommended that the Administration develop a process to select a limited number of functions currently performed by federal employees to become HPOs, and then evaluate their performance. Then, the authorized HPOs would be exempt from competitive sourcing studies for a designated period of time. Overall, however, the HPO process is intended to be used in conjunction with, not in lieu of, public-private competitions. The successful implementation of the HPO concept will require a high degree of cooperation between labor and management, as well as a firm

commitment by agencies to provide sufficient resources for training and technical assistance. In addition, a portion of any savings realized by the HPO should be available to reinvest in continuing reengineering efforts and for the HPO to use for further training and/or for incentive purposes. Let me speak specifically to the creation of HPOs. Many organizations in the past, for various reasons, have found it difficult to become high-performing organizations. Moreover, the federal government continues to face new challenges in making spending decisions for both the long and near term because of federal budget constraints, rapid advances in technology, the impending human capital crisis, and new security challenges brought on by the events of September 11, 2001. Such a transformation will require that each organization reverse decades of underinvestment and lack of sustained attention to maintaining and enhancing its capacity to perform effectively.

The Panel recognized that incentives are necessary to encourage both management and employees to promote the creation of HPOs. It envisioned that agencies would have access to a range of financial and consulting resources to develop their plans, with the costs offset by the savings realized. The Panel's report focused primarily on HPOs in the context of commercial activities, given its legislative charter. However, there is no reason why the concept could not be applied to all functions, since much of the government's work will never be subject to competition.

HPOs may require some additional flexibility coupled with appropriate safeguards to prevent abuse. The Panel also envisioned the use of performance agreements and periodic performance reviews to ensure appropriate transparency and accountability.

Although a minority of the Panel did not support the package with the three additional recommendations noted above, some of them indicated that they supported one or more elements of the package. Importantly, there was a good faith effort, even at the last minute of the report's preparation, to maximize agreement and minimize differences between Panelists. In fact, changes were made even when it was clear that some Panelists seeking changes were highly unlikely to vote for the supplemental package of recommendations. As a result, on the basis of Panel meetings and my personal discussions with Panel members at the end of our deliberative process, the major differences between the Panelists were few in number and philosophical in nature. Specifically, disagreement centered primarily on the (1) recommendation related to the role of cost in the new FAR-type process and (2) the number of times the Congress should be required to act on the new integrated process,

including whether the Congress should specifically authorize a pilot program that tests that process for a specific time period.

Implementation Strategy

Many of the Panel's recommendations can be accomplished administratively under existing law, and the Panel recommends that they be implemented as soon as practical. The Panel also recognizes that some of its recommendations would require changes in statutes or regulations and that making the necessary changes could take some time. Any legislative changes should be approached in a comprehensive and considered manner rather than a piecemeal fashion in order for a reasonable balance to be achieved. Like the guiding principles, the recommendations were the result of much discussion and compromise and should be considered as a whole.

Moreover, although the Panel views the use of a FAR-type process for conducting public-private competitions as the end state, the Panel also recognizes that some elements of its recommendations represent a shift in current procedures for the federal government. Therefore, the Panel's report outlined the following phased implementation strategy that would allow the federal government to demonstrate and then refine its sourcing policy on the basis of experience:

- A-76 studies currently under way or initiated during the near term should continue under the current framework. Subsequent studies should be conducted in accordance with the improvements listed in our report. OMB should develop and oversee the implementation of a FAR-type, integrated competition process. In order to permit this to move forward expeditiously, it may be advisable to limit the new process initially to civilian agencies where, except for allowing protests by federal employees, its use would not require legislation. Statutory provisions applying only to DOD agencies may require repeal or amendment before the new process could be used effectively at DOD, and the Panel recommends that any legislation needed to accommodate the integrated process in DOD be enacted as soon as possible. As part of a phased implementation and evaluation process, the Panel recommends that the integrated competition process be used in a variety of agencies and in meaningful numbers across a broad range of activities, including those currently performed by federal employees, work currently performed by contractors, and new work.
- Within 1 year of initial implementation of the new process, and again 1 year later, the Director of OMB should submit a detailed report to the Congress identifying the costs of implementing the new process, any savings expected to be achieved, the expected gains in efficiency or

effectiveness of agency programs, the impact on affected federal employees, and any lessons learned as a result of the use of this process together with any recommendations for appropriate legislation.

- GAO would review each of these OMB reports and provide its independent assessment to the Congress. The Panel anticipates that OMB would use the results of its reviews to make any needed “mid-course corrections.” On the basis of the results generated during the demonstration period, and on the reports submitted by OMB and GAO, the Congress will then be in a position to determine the need for any additional legislation.

Conclusions

The federal government is in a time of transition, and we face a range of challenges in the 21st century. This will require the federal government to transform what it does, the way that it does business, and who does the government’s business in the 21st century. This may require changes in many areas, including human capital and sourcing strategies. On the basis of our statutory mandate, the Commercial Activities Panel primarily focused on the sourcing aspects of this needed transformation.

I supported the adoption of the set of principles as well as the package of additional recommendations contained in the Panel’s report. Overall, I believe that the findings and recommendations contained in the Panel’s report represent a reasoned, reasonable, fair, and balanced approach to addressing this important, complex, and controversial area. I hope that the Congress and the Administration will consider and act on this report and its recommendations in a timely manner. I particularly want to urge the Congress and the Administration to consider the importance of encouraging agencies to become high-performing organizations on an ongoing basis. Agencies should not wait until faced with the challenge of public-private competitions to seek efficiencies to retain work in-house. In addition, most of government’s workers will never be subject to competitions. As a result, I believe that the Panel’s recommendation pertaining to high-performing organizations could be an important vehicle for fostering much needed attention to how we enhance the economy, efficiency, and effectiveness of the federal government in ways other than through competition.

Finally and most importantly, in considering the Panel’s package of recommendations or any other changes that may be considered by the Congress and the Administration, the guiding principles, developed and unanimously agreed upon by the Panel, should be the foundation for any future action.

Let me also add that I appreciate the hard work of my fellow Panelists and their willingness to engage one another on such a tough issue—one where we found much common ground despite a range of divergent views. I also want to thank the GAO staff and the other support staff who contributed to this effort. The Panel has completed its work. It is time for the Congress and OMB to act on our report.

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to any questions that you or other members of the subcommittee may have.

Appendix I: Members of the Commercial Activities Panel

David M. Walker, Chairman,
Comptroller General of the United States

E. C. "Pete" Aldridge, Jr.,
Under Secretary of Defense for Acquisition,
Technology and Logistics

Frank A. Camm, Jr.,
Senior Analyst, RAND

Mark C. Filteau,
President, Johnson Controls
World Services, Inc.

Stephen Goldsmith,
Senior Vice President, Affiliated
Computer Services

Bobby L. Harnage, Sr.,
National President, American Federation
of Government Employees, AFL-CIO

Kay Cole James,
Director, U.S. Office of Personnel Management

Colleen M. Kelley,
National President, National Treasury Employees Union

The Honorable David Pryor,
Director, Institute of Politics, Harvard University

Stan Z. Soloway,
President, Professional Services Council

Angela B. Styles,¹
Administrator, Office of
Federal Procurement Policy

Robert M. Tobias,
Distinguished Adjunct Professor,
American University

¹ Angela Styles replaced Sean O'Keefe on the Commercial Activities Panel in December 2001 after he was confirmed as the Administrator of the National Aeronautics and Space Administration.

Appendix II: Summary of Commercial Activities Panel Public Hearings

Washington, D.C., June 11, 2001 “Outsourcing Principles and Criteria”

Key Points

- Status quo is not acceptable to anyone.
- Sourcing decisions require a strategic approach.
- Federal workers should perform core government functions.
- Need for MEOs throughout the government.
- Government needs clear, transparent, and consistently applied sourcing criteria.
- Avoid arbitrary FTE goals.
- Objective should be to provide quality services at reasonable cost.
- Provide for fair and efficient competition between the public and private sectors.
- Sourcing decisions require appropriate accountability.

Indianapolis, Indiana, August 8, 2001 “Alternatives to A-76”

Key Points

- Crane Naval Surface Warfare Center’s reengineering process led to significant efficiencies and reduced workforce trauma.
- Employees must be involved with any reform effort. Secrecy is counterproductive.
- Committed leadership, effective implementation, and well-planned workforce transition strategies are key to any reform effort.
- Privatization-in-place was used effectively at Indianapolis Naval Air Warfare Center to avert a traditional Base Realignment and Closure action.
- The city of Indianapolis provided certain technical and financial assistance to help workers successfully compete for the work.
- Certain technology upgrades in Monterey, California, via a public-private partnership led to efficiencies and increased effectiveness.
- Measuring performance is critical.
- A-76 is only one of many efficiency tools available to federal managers.
- Other tools include
 - Bid to goal, which helps units become efficient and thus avoid A-76,
 - Transitional Benefit Corporation, a concept that promotes the transfer of government assets to the private sector and provides transition strategies for employees, and

- ESOP, under which employees own a piece of the organization that employs them. ESOPs have been established in a few federal organizations.

San Antonio, Texas, August 15, 2001
“A-76, What’s Working and What’s Not”

Key Points

- A-76 process is too long and too costly.
- Cost of studies can greatly reduce government savings.
- Cost to industry in both dollars and uncertainty.
- Demoralized workers quit. But successful contractors need these workers.
- Larger A-76 studies can yield greater savings, but these studies become much more complex.
- Lack of impetus for savings without competition.
- One-step bidding process should be used.
- MEO and contractors should
 - Compete together in one procurement action,
 - Be evaluated against the same solicitation requirements using the same criteria, and
 - Be awarded contracts based on best value.
- Provide more training for MEO and A-76 officials.
- MEOs should have legal status to protest and appeal awards and obtain bid information.
- A-76 rules should be more clear and applied consistently through a centralized management structure.
- For bid and monitoring purposes, government costs should be collected and allocated consistent with industry (e.g., activity-based costing).
- Need to eliminate any suggestion of conflicts of interest.
- Need incentives for agencies and workers (e.g., share-in-savings).
- Provide soft landings for workers.
- Allow workers to form public-sector organizations for bidding.

Appendix III: Sourcing Principles¹

Based on public input, a review of previous studies and other relevant literature, and many hours of deliberation, the Panel developed and unanimously adopted a set of principles that it believes should guide sourcing policy for the federal government. While each principle is important, no single principle stands alone. As such, the Panel adopted the principles as a package. The Panel believes that federal sourcing policy should:

1. Support agency missions, goals, and objectives.

Commentary: This principle highlights the need for a link between the missions, goals, and objectives of federal agencies and related sourcing policies.

2. Be consistent with human capital practices designed to attract, motivate, retain, and reward a high-performing federal workforce.

Commentary: This principle underscores the importance of considering human capital concerns in connection with the sourcing process. While it does not mean that agencies should refrain from outsourcing due to its impact on the affected employees, it does mean that the federal government's sourcing policies and practices should consider the potential impact on the government's ability to attract, motivate, retain, and reward a high-performing workforce both now and in the future. Regardless of the result of specific sourcing decisions, it is important for the workforce to know and believe that they will be viewed and treated as valuable assets. It is also important that the workforce receive adequate training to be effective in their current jobs and to be a valuable resource in the future.

3. Recognize that inherently governmental and certain other functions should be performed by federal workers.

Commentary: Recognizing the difficulty of precisely defining "inherently governmental" and "certain other functions," there is widespread consensus that federal employees should perform certain types of work. Office of Management and Budget (OMB) Directive 92-1 provides a framework for defining work that is clearly "inherently governmental" and

¹ The sourcing principles were taken in their entirety from *Commercial Activities Panel, Improving the Sourcing Decisions of Government: Final Report* (Washington, D.C.: April 2002).

the Federal Activities Inventory Reform (FAIR) Act has helped to identify commercial work currently being performed by the government. It is clear that government workers need to perform certain warfighting, judicial, enforcement, regulatory, and policymaking functions, and the government may need to retain an in-house capability even in functions that are largely outsourced. Certain other capabilities, such as adequate acquisition skills to manage costs, quality, and performance and to be smart buyers of products and services, or other competencies such as those directly linked to national security, also must be retained in-house to help ensure effective mission execution.

4. Create incentives and processes to foster high-performing, efficient, and effective organizations throughout the federal government.

Commentary: This principle recognizes that, historically, it has primarily been when a government entity goes through a public-private competition that the government creates a “most efficient organization” (MEO). Since such efforts can lead to significant savings and improved performance, they should not be limited to public-private competitions. Instead, the federal government needs to provide incentives for its employees, its managers, and its contractors to constantly seek to improve the economy, efficiency, and effectiveness of the delivery of government services through a variety of means, including competition, public-private partnerships, and enhanced worker-management cooperation.

5. Be based on a clear, transparent, and consistently applied process.

Commentary: The use of a clear, transparent, and consistently applied process is key to ensuring the integrity of the process as well as to creating trust in the process on the part of those it most affects: federal managers, users of the services, federal employees, the private sector, and the taxpayers.

6. Avoid arbitrary full-time equivalent (FTE) or other arbitrary numerical goals.

Commentary: This principle reflects an overall concern about arbitrary numbers driving sourcing policy or specific sourcing decisions. The success of government programs should be measured by the results achieved in terms of providing value to the taxpayer, not the size of the in-house or contractor workforce. Any FTE or other numerical goals should be based on considered research and analysis. The use of arbitrary percentage or numerical targets can be counterproductive.

7. Establish a process that, for activities that may be performed by either the public or the private sector, would permit public and private sources to participate in competitions for work currently performed in-house, work currently contracted to the private sector, and new work, consistent with these guiding principles.

Commentary: Competitions, including public-private competitions, have been shown to produce significant cost savings for the government, regardless of whether a public or a private entity is selected. Competition also may encourage innovation and is key to improving the quality of service delivery. While the government should not be required to conduct a competition open to both sectors merely because a service could be performed by either public or private sources, federal sourcing policies should reflect the potential benefits of competition, including competition between and within sectors. Criteria would need to be developed, consistent with these principles, to determine when sources in either sector will participate in competitions.

8. Ensure that, when competitions are held, they are conducted as fairly, effectively, and efficiently as possible.

Commentary: This principle addresses key criteria for conducting competitions. Ineffective or inefficient competitions can undermine trust in the process. The result may be, for private firms (especially smaller businesses), an unwillingness to participate in expensive, drawn-out competitions; for federal workers, harm to morale from overly long competitions; for federal managers, reluctance to compete functions under their control; and for the users of services, lower performance levels and higher costs than necessary. Fairness is critical to protecting the integrity of the process and to creating and maintaining the trust of those most affected. Fairness requires that competing parties, both public and private, or their representatives, receive comparable treatment throughout the competition regarding, for example, access to relevant information and legal standing to challenge the way a competition has been conducted at all appropriate forums, including the General Accounting Office and the United States Court of Federal Claims.

9. Ensure that competitions involve a process that considers both quality and cost factors.

Commentary: In making source selection decisions in public-private competitions: (a) cost must always be considered; (b) selection should be based on cost if offers are equivalent in terms of non-cost factors (for

example, if they offer the same level of performance and quality); but (c) the government should not buy whatever services are least expensive, regardless of quality. Instead, public-private competitions should be structured to take into account the government's need for high-quality, reliable, and sustained performance, as well as cost efficiencies.

10. Provide for accountability in connection with all sourcing decisions.

Commentary: Accountability serves to assure federal workers, the private sector, and the taxpayers that the sourcing process is efficient and effective. Accountability also protects the government's interest by ensuring that agencies receive what they are promised, in terms of both quality and cost, whether the work is performed by federal employees or by contractors. Accountability requires defined objectives, processes, and controls for achieving those objectives; methods to track success or deviation from objectives; feedback to affected parties; and enforcement mechanisms to align desired objectives with actual performance. For example, accountability requires that all service providers, irrespective of whether the functions are performed by federal workers or by contractors, adhere to procedures designed to track and control costs, including, where applicable, the Cost Accounting Standards. Accountability also would require strict enforcement of the Service Contract Act, including timely updates to wage determinations.